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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

November 6, 1995

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
Room 222
1919 M Street NW
Washington, D.C. 20554

DOCKET FILE COPY ORIGINAL

Re: Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, CC Docket No. 94-1

Dear Mr. Caton:

Enclosed for filing is an original and four (4) copies of MCI Telecommunications Corporation's Petition for Reconsideration in the above-captioned rulemaking proceeding.

Please acknowledge receipt by affixing an appropriate notation on the copy of the MCI pleading furnished for such purpose and remit same to bearer.

Sincerely,

Mary L Brown

Mary L. Brown

No. of Copies rec'd 0+4
List A B C D E

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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OFFICE OF SECRETARY

In the Matter of	)	
	)	
Price Cap Performance Review	)	CC Docket No. 94-1
for Local Exchange Carriers;	)	
Treatment of Video Dialtone Services	)	
Under Price Cap Regulation	)	

Petition for Reconsideration

MCI Telecommunications Corporation ("MCI") hereby petitions the Commission for reconsideration of the Second Report and Order in this phase of the price cap performance review proceeding, which is limited to the regulatory treatment of local exchange carriers' ("LECs") video dialtone services.[1] MCI finds the adoption of a "de minimis" standard that would exempt LECs from cost allocation requirements to contradict existing Commission cost allocation systems, require costly and cumbersome auditing procedures to enforce, and will likely to permit video dialtone carriers to cross subsidize their video dialtone offerings with revenue from other common carrier services. In addition, MCI is unable to discern any administrative savings from this proposal, contrary to the rationale given in the Order. MCI also requests reconsideration of the decision not to address the need for a Part 69 element. While the Order claimed that this issue was "beyond the scope" of this proceeding, the

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[1] Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, CC Docket No. 94-1, Second Report and Order and Third Further Notice of Proposed Rulemaking, FCC 95-394, released September 21, 1995 (Second Report and Order).

Part 69 issue is integral to the formulation of a Price Cap basket and the Commission's stated intention to protect ratepayers.

In deciding to segregate video dialtone rates in a separate video dialtone price caps basket, the Commission decided that costs and revenues should be separated. This is necessary, the Commission found, in order to ensure that the sharing and low end adjustment mechanism under price caps is not affected by video dialtone costs and revenues. MCI agrees with these findings. However, the Commission decided that, at any level above a de minimis amount, video dialtone costs and revenues should be separated from existing Part 69 access elements for the purposes of reporting costs and revenues of telephony. Further, the Order declined to create a separate Part 69 rate element to which video dialtone costs could be assigned.[2]

A De Minimis Threshold Is Inconsistent With Commission Cost Allocation Policy

As stated in MCI's earlier-filed comments in the Third Notice in this docket,[3] MCI opposes the de minimis threshold that would trigger cost allocation reporting. Nowhere in the Commission's cost reporting and allocation rules is there a rule which allows carriers to forgo cost allocation practices because an amount is deemed "too small." The Uniform System of Accounts (Part 32) requires all costs to be recorded. The Part

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[2] Second Report and Order at paras. 35-38.

[3] MCI Comments on the Third Further Notice of Proposed Rulemaking, CC Docket No. 94-1, filed October 27, 1995.

64 separation of nonregulated costs and affiliate transaction rules contain no such de minimis exemption. Jurisdictional separations (Part 36) similarly requires all regulated costs to be separated. Most importantly, the Part 69 access rules serve to allocate all of the interstate revenue requirements to Part 69 rate elements. The notion that there may be video dialtone costs that are "too small" to be worthy of a cost allocation process is antithetical to the entire history of common carrier cost allocation theory at the Commission.

Specifically, the Commission's cost allocation system has relied exclusively on fully distributed costing. This is to be distinguished from incremental costing methods which are permitted under tariff regulations and which are used for pricing purposes. Under price caps, the cost allocation rules up through and including Part 69 are used exclusively for reporting and monitoring of carrier investments, expenses, and revenues.

The reason for the use of fully distributed costing methodologies is stated most concisely in the Commission's decision inaugurating a Part 64 process to separate the cost of regulated and nonregulated activities. There, the Commission noted that it had two reasons for the decision to employ fully distributed costing methods -- (1) the prevention of cross-subsidy; and (2) allowing ratepayers to reap some of the benefits of the economies of scale and scope that come from a carrier's participation in nonregulated activities. The Commission found that "it would not be just and reasonable to allow all of those economies to belong to the nonregulated activities."[4] The public policy guiding LEC participation in nonregulated activities is no different in the context of LEC participation in video dialtone.

Inconsistency with the entire body of Commission cost allocations is only one reason to avoid the use of a de minimis standard. By requiring carriers participating in video dialtone to separate all video dialtone costs from telephony -- and not just some of those costs -- the Commission avoids the heavy burden of having to monitor and audit LEC accounting practices to ensure that its rules are being followed. The recent release of the Lobbying Expenses audit should give policymakers pause in allowing the LECs flexibility in deciding when cost allocations should be performed.[5]

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[4] Separation of costs of regulated telephone service from costs of nonregulated activities, CC Docket No. 86-111, Report and Order, 2 FCC Rcd 1298, 1312 (1987).

[5] On October 26, 1995, the Common Carrier Bureau released a summary of its audit of Bell Operating Company (BOC) lobbying costs. The Commission's rules require the BOCs to exclude lobbying costs from their interstate telephone costs. The summary explains that, prior to the audit, the BOCs recorded only minimal lobbying costs in the correct manner. For example, the auditors found that two BOCs had limited the definition of lobbying to encompass only face-to-face contacts with legislators that lasted an hour and attempted to influence them on legislation. The auditors also found that most BOCs had misclassified the costs of lobbying-related clerical and staff support, travel, and overheads as operating expenses. Auditors also concluded that all of the BOCs had failed to record any portion of their dues to the United States Telephone Association, which had lobbied on behalf of the BOCs. They further found that certain BOCs have financed the publication of articles as part of their lobbying efforts without recording the associated costs in Account 7370. Summary of Lobbying Cost Audit Findings, Report No. CC 95-65, Common Carrier Action, released October 26, 1995 at 2.

Lax regulation that allows cross subsidy in any amount is bad public policy. LEC telephone costs and revenues should be reported separately from video dialtone costs and revenues in order to ensure that the Commission always has an accurate picture of LEC performance. Whether sharing is ultimately discarded by the Commission as a ratepayer-protection device, the Commission will nonetheless have an ongoing need to understand LEC financial performance in telephony in isolation from nonregulated activities and video dialtone.

There Is No Savings of Administrative "Burden" in Forestalling Cost Reporting Since the Carrier Must Track Costs To Comply With Threshold Rule

MCI believes that the Order's stated rationale for creating the "de minimis" standard does not support its decision. According to the Order, requiring LECs to separate video dialtone costs and revenues in the early years of video dialtone services will be "an unnecessary administrative burden."[6] The Order states that only when costs and revenues grow in size enough to have an effect on sharing and low-end adjustments should separation be required.

Since the Order makes clear that LECs will be required to report video dialtone costs and revenues separately for the purposes of calculating overall LEC earnings levels, and since that calculation requirement will be implemented at some point to be determined by the Third Further Notice in this docket, the LECs have an immediate

[6] Second Report and Order at para. 35.

obligation to track video dialtone costs and revenues for the purpose of determining the point at which the "de minimis" standard is met and exceeded. This internal tracking obligation is necessary to the functioning of the "de minimis" standard adopted in the Order. Without tracking this information now, the LEC could not hope to comply with the Commission's requirement.

If the tracking of costs and revenues is already implicitly required by the Order, then the additional "administrative burden" that the Order refers to can only mean the year-end calculation of earnings. The administrative "burden" placed on a LEC to subtract video dialtone costs and revenues from total cost and revenues is so infinitesimal as to be nonexistent. MCI can find no "burden" on the LEC to exclude video dialtone costs and revenues from telephony earnings.

A Part 69 Rate Element Is Necessary for Accurate Cost Accounting

MCI fully agrees with the Commission's intention to exclude video dialtone activities from LEC earnings calculations in order to ensure that price cap regulation is not distorted by video dialtone investment. The Second Report and Order, by creating a separate price cap basket and requiring cost accounting mechanisms to segregate telephony from video dialtone, are steps that will be of some assistance in protecting telephone ratepayers from cost-shifting. However, MCI remains perplexed at the continuing dismissal of its arguments that the Commission create a separate Part 69 rate element for video dialtone. Without the designation of a Part 69 rate element into which video dialtone costs can be placed, the LECs will have the flexibility to associate video dialtone costs with other Part 69 telephony rate elements -- in spite of the existence of well-meaning cost allocation requirements or monitoring proposals.[7]

A video dialtone Part 69 element would serve the same purpose as the existing special access element or Interexchange element -- it would create a Part 69 "bucket" for costs to be allocated to, without prescribing a specific rate structure for the video dialtone services that a LEC will tariff. Absent the creation of a video dialtone element in Part 69, video dialtone will be treated differently from any other service offering the LECs provide. The Commission has to date given no cogent reason for declining to adopt a Part 69 element.

In the Third Further Notice in this docket, the Commission has requested comment on adoption of a Part 69 allocator that would serve to separate video dialtone costs that exceed the threshold. The Commission has correctly recognized that cost allocation requirements are essential to protect telephone ratepayers from cost-shifting. Yet the Second Report and Order states that creating a Part 69 rate element is "beyond the scope" of this proceeding. Since the function of a Part 69 element is fundamentally to allocate costs, the rationale provided by the Second Report and Order must be

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[7] See, e.g., Summary of Lobbying Cost Audit Findings, Report No. CC 95-65, October 26, 1995 (despite the existence of a clear rule requiring that lobbying expenses be accounted for outside the rate base, the Bell Operating Companies recorded $116.5 million of lobbying expenses as a regulated item).

wrong. The Commission should reconsider this decision, and create a Part 69 element for video dialtone.

Conclusion

For the foregoing reasons, MCI urges the Commission to reconsider its decision to establish a de minimis threshold requirement for exclusion of video dialtone costs and revenues from telephony earnings. MCI further urges the Commission to establish a Part 69 element for video dialtone.

Respectfully submitted,

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Date: November 6, 1995

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